

## Cambridge, Massachusetts

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### Credit Profile

US\$69.885 mil GO bnds (mun purp loan of 2008) dtd 02/01/2008 due 02/01/2009-2028

<b>Long Term Rating</b>	AAA/Stable	New
Cambridge GO		
<b>Long Term Rating</b>	AAA/Stable	Affirmed

### Rationale

Standard & Poor's Ratings Services assigned its 'AAA' rating, with a stable outlook, to Cambridge, Mass.' series 2008 GO bonds.

At the same time, Standard & Poor's affirmed its 'AAA' rating on the city's GO parity debt. The outlook is stable.

The rating reflects the city's:

- Dynamic local economy, which is centered on Harvard University and the Massachusetts Institute of Technology (MIT);
- Above-average wealth and income factors, including a high market value per capita;
- Strong financial position, due to an experienced management team, and strong management policies; and
- Below-average debt burden and manageable capital plan.

The city's full faith and credit pledge secures the bonds. Officials will use bond proceeds for various capital projects.

Cambridge, with a stable population of 101,355, is across the Charles River from Boston, Mass. ('AA' GO debt rating, stable outlook). Anchored by the intellectual capital of Harvard University and MIT, the local economy is strong and concentrated in high-tech, biotechnology, engineering, medicine, education, and consulting. The city's 2006 unemployment rate of 3.4% remains below the commonwealth (5.0%) and nation (4.6%). Wealth and income factors are

also high; according to 2005 U.S. Department of Commerce statistics, the city's income of \$51,869 per capita was 120% of the commonwealth's average and 151% of the nation's average.

Cambridge continues to experience strong economic activity driven, in large part, by a growing pharmaceutical and biotechnology sector spun off from both universities. Since 2005, the city's assessed valuation (AV) has grown by 10.2%, totaling \$23.5 billion in fiscal 2008. The full market value of properties is currently a very high \$242,015 per capita, which is a reflection of the strong commercial and industrial base, accounting for 36% of total valuation. Ongoing redevelopment projects should ensure continued tax base growth over the next several years. Based on new construction estimates and the appreciation of values of existing property, city officials estimate the tax base will continue to grow at an average annual rate of 3% through 2012.

Cambridge's financial performance and position remains strong and stable, partly due to the city's fiscal management and policies. The city closed unaudited fiscal 2007 with its eighth consecutive general fund surplus, increasing unreserved fund balance to a sound \$134.8 million, or 35% of expenditures. Additional reserves, liquidity, and property tax levy capacity further strengthen the city's already strong financial position. The city's stabilization, health claims trust, and parking funds provide \$52.7 million of added revenue flexibility. In addition, the city maintains a large unused tax levy capacity totaling \$88.3 million (36% of gross tax levy). The excess levy capacity allows city officials to appropriate that amount, if needed, for operations or capital without the need for electorate-approved exemptions or overrides.

The 2008 budget of \$412 million is balanced and is an increase of 3.7% from the previous year. Property taxes are the leading revenue source, representing 62% of general fund revenues; tax collections remain strong, averaging 98% to 99% on a current-year basis. We consider Cambridge's management practices strong under our Standard & Poor's Financial Management Assessment (FMA). An FMA of strong indicates that practices are strong, well embedded, and likely sustainable.

Cambridge's debt profile is also favorable. Net of self-supporting water and sewer debt and state school construction reimbursements, net debt is an average \$2,108 per capita, or a low 0.8% of market value. Even factoring in the \$108 million unfunded pension liability as debt, debt ratios remain a moderate \$3,176 per capita and just 1.3% of market value. The city's carrying charge is also low, with debt service expenditures historically less than 10% of total expenditures. Amortization of debt is very rapid, with 51% of principal outstanding to be retired over five years and 79% to be retired over 10 years.

### ***Outlook***

The stable outlook reflects the expectation that the city will continue to manage its financial position prudently, which it has significantly demonstrated by increasing reserves over the past eight years. The city's economic and property tax base development is expected to continue, allowing it to maintain structural balance between revenues and expenditures while maintaining ample tax levy flexibility.

### ***Economy: Diverse, With Continued Tax Base Growth***

Cambridge's local economy is strong and concentrated in high-tech, biotechnology, engineering, medicine, education, finance, and management consulting. The city remains a net importer of jobs; in 2007, there were 104 positions for every 100 city residents. Harvard and MIT are the city's two leading employers in addition to being a stabilizing factor, accounting for 18% of the city's workforce.

Leading employers include:

- Harvard (10,031 employees);
- MIT (8,044);
- Cambridge (2,857);
- Mount Auburn Hospital (1,875);
- Cambridge Health Alliance (1,436);
- Federal government (1,426), primarily the transportation research center; and
- Biogen (1,543).

Cambridge is also home to a concentrated cluster of world-recognized biotechnology and pharmaceutical firms. The concentration of intellectual capital at Harvard and MIT and R&D think tank Whitehead Institute (500 employees) is attractive to this sector. Private biotechnology firms account for six of the city's 25 leading employers.

They are:

- Biogen (1,543 employees),
- Novartis (1,399),
- Genzyme (1,388),
- Millennium Pharmaceuticals Inc. (932),
- Vertex Pharmaceuticals (894), and
- Wyeth Cambridge (684).

Cambridge, with just 6.26 square miles, has historically had to rely on redevelopment for new growth. The city's property tax base reached \$23.5 billion in fiscal 2008, up 6.2% from fiscal 2007 and 10.2% higher than 2005 values. Ongoing and planned projects should ensure continued tax base growth over the next several years. One such project is the redevelopment of North Point, a 60-acre former railroad parcel with excellent highway access located across the Charles River from Boston's North Station. The North Point project, which began in 2005, has a 15- to 20-year buildout, and will essentially create a new neighborhood within the city. The development will include 2.2 million square feet of commercial and R&D space and 2,400-2,700 housing units.

### ***Finances: Stable And Strong***

Following its eighth consecutive operating surplus in fiscal 2007, Cambridge's financial position remains strong. The unreserved general fund balance totaled \$134 million, or 35% of expenditures, in fiscal 2007. Over the past three years, the city's unreserved balances have averaged 33% of expenditures, above the national average for similar-sized municipalities and above average compared with other 'AAA'-rated cities and towns. In addition, the city's stabilization, health claims trust, and parking funds provide \$52.7 million of added revenue flexibility. The local property tax, which now accounts for 62% of total revenues, is the city's leading revenue source. Cambridge's operations are not susceptible to future state aid cuts, as the city derives roughly 13% of general fund revenues from intergovernmental sources. Cambridge bills property taxes semiannually; current-year collections remain strong, typically averaging 98%-99% of the levy.

Over the years, fueled by continued growth in the tax base and increases in new residential and commercial assessed valuations, the city has built a large unused tax levy capacity. The excess levy allows city officials to appropriate that amount, if needed, for operations or capital without the need for electorate-approved exemptions or overrides allowed under Proposition 2 1/2 constraints. In fiscal

2008, the city maintained roughly \$88.3 million (36% of gross tax levy) of unused tax levy capacity, which is the largest level maintained in the commonwealth. The fiscal 2008 budget totals \$412 million, or a 3.8% increase from 2007 levels.

### ***Financial Management Assessment: 'Strong'***

Standard & Poor's revised its FMA to strong from good following the city's adoption of a formal reserve policy and debt management policy. An FMA of strong indicates that practices are strong, well embedded, and likely sustainable. The reserve policy limits the total fund equity and the unreserved general fund to 25% and 15% of ensuing fiscal year operating revenues, respectively. The adopted debt management policy limits debt service to 12.5% of budget and principal amortization to 70% within 10 years. In addition, the city's overall net debt per capita should not exceed 4.5% of per capita personal income and 1.5% of estimated full AV.

Additional highlights factoring into the strong assessment include:

- Monthly budget surveillance that compares budgeted expenditures with five-year budgeted actuals;
- A formal five-year budget and financial plan that is based on conservative revenue and expenditure assumptions; and
- A five-year public investment improvement program, in which management identifies projects and funding sources and links them to the city's five-year financial plan.

### ***Debt And Other Fixed Liabilities***

Cambridge's five-year public improvement program totals \$180 million of capital needs through 2012. City officials have identified roughly \$136 million of water and sewer needs, accounting for about 75% of the total plan. The city plans to use Massachusetts Water Resources Authority grants to fund a large portion of this amount. Officials also plan to issue additional debt to fund roughly 40% of the total plan. After the sale of this issuance, the city will be left with roughly \$101.5 million in authorized, but unissued, debt. The future debt burden will remain manageable, as city officials will continue to finance future outlays in accordance with the city's debt management plan.

The city's \$108 million unfunded pension liability, dated Jan. 1, 2006, accounts for a nearly 85% funded ratio, well above the city's commonwealth peers and above average compared with its national peers. The city is on schedule to fully fund its pension system by 2015. The city completed an actuarial valuation of other postemployment benefits (OPEB) in 2007. The city's valuation report shows a range of liabilities that reflect both prefunding and pay-as-you-go funding. It also includes estimates under two different funding methods: projected unit credit (used by the city's retirement system) and entry age normal (the cost method required under FASB Statement 106). At July 1, 2007, if prefunding is assumed, the liability ranges from \$352 million (entry age normal) to \$365 million (projected unit credit). If a pay-as-you-go approach is assumed, the liability ranges from \$553 million (entry age normal) to \$603 million (projected unit credit). The city will comply with GASB 45 reporting requirements in fiscal 2008. Cambridge's pay-as-you-go OPEB amounted to \$14 million in fiscal 2007, or about 4% of fiscal 2007 general fund expenditures. The city's actuarial required contribution ranges from \$27 million to \$44 million, depending on the amortization and funding option selected.

Tax Supported  
New Issue

# Cambridge, Massachusetts

## Ratings

New Issue	
General Obligation (GO) Municipal Purpose Loan of 2008 Bonds	AAA
Outstanding Debt	
GO Bonds	AAA

## Rating Outlook

Stable

## Analysts

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## New Issue Details

**Sale Information:** \$69,885,000 GO Municipal Purpose Loan of 2008 Bonds, scheduled to sell competitively on Feb. 5.  
**Security:** GOs of the city of Cambridge, payable from taxes levied on all taxable property, subject to statutory levy limitations.  
**Purpose:** Fund various capital improvement projects in the city.  
**Final Maturity:** Due serially Feb. 1, 2009–2028. Interest payable each Feb. 1 and Aug. 1, beginning Aug. 1, 2008.

## Related Research

- *Cambridge, Massachusetts, Jan. 29, 2007*
- *Local Government General Obligation Rating Guidelines, March 22, 2007*

## Rating Rationale

- The longstanding presence of higher education, health care, biotechnology, and life sciences industries creates a stable, well-diversified economy.
- Exceptional financial management reflected in consistently strong financial results and reserve levels.
- Debt levels are expected to remain manageable given the city's limited capital needs.

## Key Rating Drivers

- Continued, strong financial management should enable Cambridge to maintain its superior credit rating.

## Credit Summary

Cambridge's well-diversified economy is characterized by favorable labor market conditions that continue to outperform those of the county, commonwealth, and nation. The November 2007 unemployment rate of 2.7% compared favorably to the 4.1% and 4.7% rates posted by the commonwealth and nation, respectively, and represented a decline of nearly a full percentage point from the prior year. There has been virtually no growth in population since the 2000 census figure of 101,355, and employment numbers have shown modest declines; however, both trends have showed signs of reversing since 2006. In particular, employment base figures grew by 1.0% in 2006 and by 1.2% between November 2006 and 2007, year over year. Income levels are high; 2006 per capita money income equaled 120% and 145% of the commonwealth and national levels, respectively. This is particularly notable given the area's large student population related to the presence of MIT and Harvard.

Exceptional financial management and planning are demonstrated by the city's strong financial position, characterized by ample reserve and liquidity levels. Audited results for fiscal 2007 show an unreserved general fund balance of \$134.9 million, totaling a high 35.9% of spending, up from 33.6% in fiscal 2006. The fiscal 2008 budget represents a modest 4% increase in spending over fiscal 2007 budgeted levels and includes the use of about \$11 million of reserves as a revenue source. The city typically budgets some use of reserves but has posted an operating surplus in each year of this decade, the result of conservative budgeting practices. Growth in the tax base has been steady at an average of 9.9% annually since fiscal 2000, and Cambridge's substantial excess levy capacity — the largest in the commonwealth — along with its considerable reserve levels, provides a degree of flexibility to manage any potential tax revenue pressures associated with the regional housing market correction.

Cambridge's direct debt burden is moderately low on a per capita basis at \$2,270 and low relative to taxable assessed value (TAV) at 0.98%. Debt levels should remain manageable given the city's limited capital needs. The city's fiscal years 2008–2012 capital improvement plan (CIP) totals an affordable \$181 million. The bulk of planned spending is for water and sewer system improvements, with a smaller amount dedicated to general government projects. About 40% of the plan will be debt funded, with the balance funded through grants, utility system user charges, and property tax revenues and free cash. Debt is amortized rapidly, with 51% and 79% of principal retired

## Rating History

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	1/24/08
AAA	Affirmed	Stable	3/6/07
AAA	Assigned	—	12/3/01

in five and 10 years, respectively. The city is reviewing options to manage its sizable other post-employment benefits (OPEB) liability, which ranges in value depending upon whether the commonwealth grants municipalities the right to create OPEB trust funds.

## Debt

### Profile

Direct debt is moderate on a per capita basis at \$2,270 but low relative to TAV at 0.98%. The latter ratio reflects the city's sizable tax base. Debt levels include \$16.5 million in outstanding general obligation (GO) bonds issued by the city for health and hospital facilities. Although the Cambridge Public Health Commission (CPHC) pays debt service on GO debt issued for hospitals, CPHC debt is included in the city's debt ratios as the city provides an operating subsidy to the CPHC. Self-support credit is given to principal retired through sewer and water fees and commonwealth school construction grants. Although the city is responsible for a portion of the Massachusetts Water Resources Authority's (MWRA) outstanding debt, the figure is not included in the overall debt calculations because the debt is self-supporting by user fees.

The city's debt burden should remain manageable given its prudent debt management and limited capital needs. Cambridge's stringent debt policies include limiting net direct debt to 1.5% of the estimated full value of taxable real properties and retiring 70% of debt within 10 years. The city meets both policies by wide margins.

### Capital Improvement Plan

Cambridge's fiscal years 2008–2012 CIP totals an affordable \$181 million and includes funding for water and sewer improvements (76%), streets and sidewalks (10%), public safety (5%), housing (3%), and other purposes (7%). Although the city is responsible for funding a portion of the capital needs of the city's school district (the remaining funding is provided through the Massachusetts School Building Authority), these demands are minimal, as a declining enrollment trend is expected to continue. Bond proceeds will be used to fund approximately 40% of the total CIP, with MWRA grants (33%), user fees and charges (7%), and free cash and property tax revenues (6%) financing the majority of the remainder.

### Pension and Other Post-Employment Benefits

The city contributes to the Cambridge Retirement System, a defined benefit public employee retirement system. The system is well funded; the actuarial value of assets represented 85.4% of the actuarial accrued liability as of Jan. 1, 2006, the most recent date for which data are available. The funded ratio declined slightly since the previous valuation, at Jan. 1, 2004, when it equaled 86.9%. The unfunded actuarial accrued liability (UAAL) increased to \$108.0 million from \$85.6 million over the two-year period. The decline in the funded ratio is attributed to poor investment returns. The city plans to make contributions in excess of the actuarially required contribution each year through fiscal 2015 with the goal of eliminating the UAAL by that time.

### Debt Statistics

(\$000)	
This Issue	69,885
Outstanding Debt	160,233
Total Direct Debt	230,118
Overlapping Debt	0
Total Overall Debt	230,118
Debt Ratios	
Direct Debt per Capita (\$) <sup>a</sup>	2,270
Overall Debt per Capita (\$) <sup>a</sup>	2,270
As % of TAV <sup>b</sup>	1.0

<sup>a</sup>Population: 101,365 (2006 estimate).

<sup>b</sup>Taxable assessed value (TAV): \$23,541,196,000 (fiscal 2008).

Cambridge's OPEB liability is sizable relative to its budget, ranging from \$352 million–\$603 million, depending upon the actuarial method and discount rate used. Massachusetts municipalities do not yet have the authority to create OPEB trust funds. In fiscal 2007, the city expended \$15.1 million for OPEB on a pay-as-you-go basis; the city's actuarially determined annual required contribution ranges from two to three times that amount, and the city has appointed a steering committee to examine funding options.

## Finances

### Financial Results and Budget

Cambridge's financial performance has been consistently strong, characterized by ample reserves and liquidity levels, as well as significant taxing capacity under Proposition 2½. Audited results for fiscal 2007 reflect an unreserved general fund balance of 35.9% of spending, up from 33.6% and 30.3% in fiscal years 2006 and 2005, respectively. The city's liquidity position remains considerable; \$74 million of certified free cash at the close of fiscal 2007 was the largest amount in the city's history. Financial policy calls for an unreserved, undesignated general fund balance equal to 15% of the ensuing year's budgeted operating revenues.

The fiscal 2008 operating budget represents a modest 4% increase in spending over fiscal 2007 budget levels. Growth in spending is attributable mainly to increases in debt service, energy, salaries, health care, and retirement costs. Enhanced spending will be funded mainly through an increase in the property tax levy of 4.6% over the fiscal 2007 level. In accordance with past budgetary practices, about \$11 million of reserves has been budgeted as a revenue source in fiscal 2008. The city typically budgets the use of reserves but finishes the fiscal year with an addition to the fund balance, the result of conservative budgeting practices. Year-to-date results indicate positive budget variances.

### General Fund Financial Summary

(\$000, Audited Fiscal Years Ended June 30)

	2003	2004	2005	2006	2007
Real and Personal Property Taxes	198,784	206,354	220,910	222,987	231,876
Intergovernmental	42,690	42,601	43,802	44,143	44,658
Other	67,371	66,813	73,470	87,691	98,588
<b>Total Revenues</b>	<b>308,845</b>	<b>315,768</b>	<b>338,182</b>	<b>354,822</b>	<b>375,122</b>
Expenditures	306,347	314,554	323,779	350,499	364,714
Net Transfers and Other Sources/(Uses)	5,908	7,374	9,879	8,097	5,579
<b>Net Surplus/(Deficit)</b>	<b>8,407</b>	<b>8,589</b>	<b>24,282</b>	<b>12,420</b>	<b>15,987</b>
<b>Total Fund Balance</b>	<b>91,384</b>	<b>99,973</b>	<b>124,254</b>	<b>136,674</b>	<b>152,661</b>
As % of Expenditures, Transfers Out, and Other Uses					
Total Fund Balance	28.6	30.5	37.6	38.2	40.7
Unreserved Fund Balance	26.7	27.6	30.3	33.6	35.9
Unreserved, Undesignated Fund Balance	26.7	27.6	30.3	33.6	35.9

Note: Numbers may not add due to rounding.

### Revenue Base

Property tax receipts are the city's main revenue source and provide budget stability. In fiscal 2007, property taxes accounted for 59.2% of general fund operating revenues and transfers in. The city has demonstrated a willingness to raise the property tax levy to offset growth in recurring expenditures. However, due to strong growth in TAV over the past decade, the tax rate has declined despite the increases in the levy. The residential tax rate

of \$7.36 per \$1,000 of TAV in fiscal 2008 declined from \$13.43 in fiscal 1998, while the commercial rate dropped to \$17.24 from \$35.98 during the same period.

Residential properties represent 61.3% of the city's fiscal 2008 tax base, commercial 23.5%, and industrial and personal property the remainder. Despite the bulk of the tax base being comprised of residential property, the tax burden is about evenly split between the residential and commercial components, with 35.1% and 39.4% of the fiscal 2008 tax levy paid by each, respectively. As part of an effort to provide tax relief to residential owners facing a more challenging housing market, the city increased the proportion of the commercial and industrial tax levy. As a result, the city estimates that approximately 93% of residential taxpayers will see a decline, no growth, or no more than a \$100 increase in their fiscal 2008 tax bill. City residents benefit from a tax exemption on all owner-occupied primary residences equal to 30% of the average value of residential property.

## Tax Base

Cambridge conducts a full revaluation of property every three years and statistical revaluations in the interim years. The interim revaluations, now required by the commonwealth, help to smooth growth in the tax base and aid in planning. The fiscal 2008 revaluation yielded a 6.2% gain over fiscal 2007's, bringing the total tax base to \$23.5 billion. Existing residential values fell by \$145 million, underscoring a weakening housing market; however, \$436 million of new construction helped boost total residential values to \$14.4 billion. The value of existing commercial property grew by \$450 million. Tax base growth has averaged 9.9% annually since fiscal 2000, but the city's financial forecast prudently projects more modest average tax base growth of 3.1% annually through fiscal 2012. Building permit numbers continue to be robust halfway through fiscal 2008.

Impressive growth related to new construction in the residential and commercial tax base has resulted in substantial excess levy capacity under Proposition 2½, the state imposed cap limiting tax levy growth to the following:

- 2½% of the full value of taxable property.
- 2½% of the prior year's maximum permitted levy (plus certain allowances).

The city's excess levy capacity for fiscal 2008 equals \$88.3 million, the highest level for any municipality in the commonwealth. The excess levy capacity has grown each year since fiscal 1995, when it equaled a slim \$498,000. The five-year financial plan projects tax base growth and levy increases that will result in excess capacity hovering at about \$85 million through fiscal 2012. Fitch notes that the city's considerable financial reserves and excess taxing capacity provide a degree of flexibility to manage any potential property tax revenue pressures associated with the regional housing market correction.

## Levy Capacity

(Fiscal Years Ending June 30)



\*The 2008 certified free cash figure is not yet available.

Some tax base concentration exists, with the 10 largest taxpayers making up 19.3% of fiscal 2008 TAV. Concern regarding the concentration is mitigated by the fact that the largest taxpayers include stable entities with a considerable amount of investment in the city. MIT and Harvard have significant taxable property holdings in Cambridge and are the first and fifth largest taxpayers, respectively. In 2005, the city renewed payment-in-lieu-of-taxes agreements (PILOTS) with MIT and Harvard for their nontaxable property; the PILOTS extend 40 and 50 years, respectively. The remainder of the top 10 taxpayers includes a mix of biotechnology and pharmaceutical companies and is rounded out by other large commercial properties and real estate development companies.

## Economy

### Overview

Cambridge is located in Middlesex County across the Charles River from the city of Boston (GO bonds rated 'AA' with a Stable Rating Outlook by Fitch Ratings). Cambridge is an important economic component of the Boston metropolitan area and Massachusetts as a whole. The city maintains its reputation as a leading center for higher education, technology, research and development — mainly in biotechnology and life sciences — and health care institutions. The 2006 population was estimated at 101,365, registering no growth since the 2000 U.S. Census, a trend not inconsistent with regional statistics.

The biotechnology and life sciences industries continue to flourish, occupying a large portion of commercial space; three of the city's largest employers are biotechnology companies. The presence of several prominent research institutions and a well-educated work force help make the city an ideal location for high-end research. Other large employers include Harvard (10,031 employees), MIT (8,044), various health care institutions, and the federal government.

### Commercial and Residential Development

The prospects for commercial and residential development are bright. Approximately 500,000 square feet of commercial real estate is reportedly under construction, and another 3 million is in the permitting stage. Major mixed-use development is occurring at the North Point site, with private investment transforming the area around an old rail yard. The site will include up to 2,700 housing units and 2.2 million square feet of commercial, research and development, and retail space when completed. As development continues, North Point will reportedly become the largest mixed-use development project in Cambridge's history. Following a dispute, the original project partners agreed to sell the project to Archon Group (a Goldman Sachs subsidiary); the deal is expected to close in early 2008. Officials report no resultant project delays.

The commercial market is strong, as indicated by low office vacancy rates. The city's third-quarter 2007 vacancy rate was 9.4% and year-to-date rates are trending below 8.0%; leasing activity is reportedly robust. Overall office vacancy rates have been declining over the past several years, nearing the Boston level and remaining well below the surrounding suburban averages.

### Employment and Wealth Indicators

Despite declines in the employment base since the beginning of the decade, Cambridge's local labor market conditions, long a strength on its credit profile, continue to outperform those of the county, commonwealth, and nation. The city's unemployment rate for 2006 equaled 3.4%, well below those of the commonwealth (5.0%) and the nation (4.6%), and the November 2007 rate registered a low 2.7%, a decline of nearly a full percentage point from the prior year. Recently, the declining trend in the employment base has shown signs of reversal; employment figures posted a 1.0% gain in 2006 and 1.2% growth from November 2006–November 2007.

Cambridge's wealth indicators are strong. By all measures, income levels are above commonwealth and national averages. Per capita money income in 2006 was 120% and 145% of the commonwealth and national averages, respectively. Furthermore, the fiscal 2008 market value per capita is very high at \$232,242, particularly significant given the tax-exempt portion of Cambridge's property base, which equals about 25% of all property in the city.

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New Issue: **Cambridge (City of) MA**

## **MOODY'S ASSIGNS Aaa TO CAMBRIDGE'S (MA) \$69 MILLION GO BONDS**

### **TOTAL OF \$329 MILLION IN RATED DEBT OUTSTANDING, INCLUDING CURRENT ISSUE**

Municipality  
MA

#### **Moody's Rating**

<b>ISSUE</b>	<b>RATING</b>
Municipal Purpose Loan of 2008	Aaa
<b>Sale Amount</b>	\$69,885,000
<b>Expected Sale Date</b>	02/15/08
<b>Rating Description</b>	General Obligation

#### **Opinion**

NEW YORK, Jan 22, 2008 -- Moody's Investors Service has assigned a Aaa rating to the City of Cambridge's \$69 million General Obligation Bonds, Municipal Purpose Loan of 2008. At this time, Moody's has also affirmed the Aaa rating assigned to the city's \$260 million in outstanding long-term general obligation debt. The bonds are secured by the city's general obligation, limited tax pledge as debt service has not been exempted from the levy limitations of Proposition 2 ½. The bonds are issued to fund the city's fiscal 2008 public investment program, which includes library construction, municipal and school building renovations and sewer and roadway reconstruction projects. The assignment of Moody's highest quality long-term rating incorporates: an exceptionally strong financial position supported by the city's seasoned and highly effective management team, a large and diverse tax base with a significant tax-exempt sector and a favorable debt profile supported by healthy enterprise systems and significant commonwealth school building aid.

### **ROBUST RESERVE LEVELS HIGHLIGHT CONSISTENTLY STRONG FINANCIAL POSITION**

Cambridge continues to maintain a very healthy financial position given a prudent fiscal strategy implemented by a strong management team, adoption of prudent fiscal policies in its fiscal 2008 budget, steady revenue streams generated by its substantial and economically vibrant tax base and a notable degree of flexibility to address future budgetary challenges. The city remains dependent primarily on local property taxes, which represented 59% of fiscal 2007 general fund revenues, and to a lesser extent on commonwealth aid, representing roughly 11% of fiscal 2007 revenues. Operations in fiscal 2007 yielded a surplus of over \$16 million, significantly lower than the \$24 million surplus from fiscal 2005 but exceeding the five-year average of \$14 million. Conservative revenue budgeting assumptions have yielded comfortable revenue surpluses of \$16 million in fiscal 2007, while tight management of expenditures has generated moderate unspent appropriations of \$7 million. The fiscal 2007 general fund balance increased to a robust \$153 million (38.9% of general fund revenues) while the most conservative measure of legally available reserves, Cambridge's "free cash" certified by the commonwealth, totaled a sound \$73.8 million (18.8% of revenues), a significant improvement from the slim \$25 million free cash (8.3% of revenues) certified in fiscal 2001.

Notably, the adopted fiscal 2008 budget institutionalizes long held informal investment, debt and reserve policies that have guided and maintained the city's financial health. Despite ongoing expenditure pressures and limited opportunities for revenue growth, Moody's expects the city to remain in compliance with its policies and to continue to issue long-range projections, incorporating reasonable revenue and expenditure growth assumptions. The fiscal 2008 budget contains a moderate overall 3.75% increase over the adjusted fiscal 2007 budget, due to ongoing expenditure pressures in several areas including salaries, pension and health insurance, energy, debt service and regional wastewater assessments. The city's budget was balanced by a 4.55% property tax levy increase as well as a total appropriation of \$11 million free cash, stabilization and overlay reserves. Despite budgeted draws on reserves, management projects that the city will produce another operating surplus, with positive variances in revenues and expenditures expected, allowing it to maintain reserve and levy capacity levels approximating those in fiscal 2007.

The city has conducted an actuarial study to value its Other Post Employment Benefit (OPEB) liability in order to comply with GASB 45 reporting deadlines. Management has identified several potential funding sources including reductions in free cash and the health claim trust fund, and diversions of the current revenue streams allocated to pensions, when this liability is retired, and health insurance as employee

contributions are adjusted upward. Despite these pressures, Moody's expects that the city's solid historical financial performance, demonstrated ability to implement prudent fiscal policies and conservative approach to forecasting will sustain Cambridge's extremely favorable financial position.

Key to Cambridge's robust financial position are strong reserve levels maintained in its Stabilization, Parking and Health Claims Trust Funds, totaling \$52.7 million in fiscal 2007. Further, in 2001 voters passed the Community Preservation Act (CPA), imposing a 3% surtax and qualifying the city to receive state matching funds; in all \$72.2 million have been appropriated or reserved since adoption. CPA funds are available to fund affordable housing, historic preservation and open space conservation and notably have enabled the development or preservation of over 2800 units of housing in the city. The city received roughly 1.9% (\$6.9 million) of revenues from Payments-In-Lieu of Taxes (PILOTs) in fiscal 2007, with the majority coming from Harvard University (rated Aaa/stable outlook) and the Massachusetts Institute of Technology (MIT, also rated Aaa/stable outlook). Both institutions own significant taxable real estate and are major taxpayers, which together represent 8.3% of Cambridge's 2008 assessed value and nearly 12% of the levy. The city has recently signed a 40-year, \$101 million agreement with MIT which increased the fiscal 2005 annual PILOT by 20%; the PILOT with Harvard was renewed for 50 years and included a one-time \$1 million payment in fiscal 2005. Each PILOT includes annual escalators on the initial base payment over the term of the agreement to provide stability and to allow long-range planning for the city.

Additional flexibility is derived from Cambridge's ample excess property tax levy capacity under Proposition 2 ½, historically maintained at robust levels and currently the highest of any Massachusetts city or town. The city's excess levy capacity reached \$88.3 million in fiscal 2008 and has grown by 113% since fiscal 2004 due to strong tax base growth and controlled expenditure growth. Levy capacity is projected to stabilize at current levels in the medium term allowing the city significant flexibility to accommodate unanticipated demands in future budget cycles. The city's conservative medium-range projections also show a planned use of up to \$9.6 million annually from the City and School Debt Stabilization Funds from fiscal 2008 through fiscal 2012, which could nearly deplete the funds, but Moody's believes the city's substantial additional reserves will continue to provide sufficient flexibility for contingencies. Overall, Moody's expects that Cambridge will retain ample capacity to accommodate expenditure increases.

#### STEADILY GROWING TAX BASE INCLUDES HIGHER EDUCATION AND BIOTECHNOLOGY INSTITUTIONS

Cambridge's sizeable equalized value of \$24.5 billion is expected to experience sustained growth, reflecting ongoing development throughout the city and moderate market value appreciation, primarily in the residential sector. Fiscal 2008 assessed values grew a healthy 6% to \$23.5 billion due to rebounding commercial and industrial valuations despite slowing residential growth. Reflecting the cooling regional real estate market, city officials project modest residential assessed valuation averaging 1.75% through fiscal 2012 and 2% commercial growth through 2012, including the conversion of commercial and industrial parcels to residential use. Since 2002, the city has added over 4.3 million square feet of commercial space and city officials report that over 3 million additional square feet of research and development space, slated for housing and biotechnology research and development, is in various stages of permitting and construction in the city's targeted economic development districts. Office vacancy rates have risen slightly to 9.4% in the third quarter of 2007 (up from 8.3% in the third quarter of 2006) after the recent opening of a 289,000 square feet on Binney Street, but are still significantly lower than the 14.3% rate for the same period in 2005 and the peak 22% in 2003. Cambridge's commercial vacancy rate lags Boston's third quarter 2007 rate of 6.1% but compares favorably to the regional suburban vacancy rate of 16.4%. Residential growth is also projected to experience moderate growth due to ongoing rehabilitation of the existing housing stock and new developments, notably the residential components of the Guilford/North Point and Cambridge Research Park developments, which together with several other projects under construction are projected to add over 1,000 rental and condominium housing units in the near term. Moody's believes that the city's near-term growth projections may be conservative as fiscal 2008 year-to-date building permit revenues of \$5.5 million have already exceeded the \$2.8 million budgeted.

Cambridge's economy benefits from the presence of Harvard and MIT—which together enroll 28,400 students and provide employment for nearly 18,000 full-time equivalent positions—and the related vibrant biotechnology employment base. Together these institutions comprise 36% of the jobs provided by the city's top 25 employers and building permits issued to the universities historically represent roughly half of the city's annual activity. Income and wealth levels are strong; despite the high student population and tax exemption of nearly one-third of the tax base, the city still maintains a solid equalized value per capita of \$241,991 and Per Capita Income of \$31,156, or 120% of the commonwealth median.

#### FAVORABLE DEBT POSITION WITH MANAGEABLE FUTURE NEEDS

Moody's expects the city's below average debt burden to remain affordable given steady anticipated tax base expansion, a sizeable level of self-supporting debt, and a rapid principal retirement schedule. The city's direct debt burden of 1.0% of equalized value rises to a moderate 1.7% after including overlapping debt from the Massachusetts Water Resources Authority (MWRA senior lien debt rated Aa2/stable outlook). Self-supporting water and sewer system debt as well as the city's pay-as-you-go funding plan, budgeted at approximately \$2 million annually, also contribute to Cambridge's favorable debt ratios. Net direct debt is retired at an above-average pace of 81.4% in 10 years. Despite the rapid amortization schedule, general fund-supported debt service claimed a moderate 8.8% of fiscal 2006 expenditures. City officials plan to issue

approximately \$161 million in debt over the next four years to fund capital projects including library and school renovations. However, with approximately half of the debt expected to be supported by user fees and commonwealth subsidies Moody's expects Cambridge's debt burden to increase modestly but to remain manageable.

## KEY STATISTICS

2005 Estimated Population (US Census): 100,365

2000 Per Capita Income: \$31,156 (120% of state median)

2007/8 Equalized Value: \$24.5 billion

2007/8 Equalized Value per Capita: \$241,991

Equalized Value Average Annual Growth 2002-2008: 11.6%

Adjusted Debt Burden: 1.7%

Amortization of principal (10 years): 81.4%

FY07 General Fund Balance: \$153 million (38.9% of General Fund revenues)

FY07 Undesignated General Fund Balance: \$136 million (34.7% of General Fund revenues)

FY07 City Stabilization Fund balance: \$14.1 million (3.6% of General Fund revenues)

FY07 School Stabilization Fund balance: \$11.6 million (2.9% of General Fund revenues)

Post-sale long-term debt outstanding: \$329 million

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